May 10, 2004

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
Office of the Secretary
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551
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Attention: Docket No. R-1186
Regulation C (Home Mortgage Disclosure Act And Regulation)

Dear Ladies and Gentlemen:

The American Financial Services Association (AFSA) appreciates the opportunity to comment on the revised formats for public disclosure of mortgage lending data issued by the Board of Governors of the Federal Reserve System. AFSA represents nearly 400 financial services companies; many of which engage in mortgage lending and are subject to Regulation C.

The Home Mortgage Disclosure Act (HMDA), enacted in 1975 and made permanent in 1988, sought to determine if potentially discriminatory practices in the area of mortgage lending were occurring. Under the law, the data reported is intended to provide information to address fair-lending concerns about loan pricing, and to gain a better understanding of the mortgage market. Unfortunately, we believe the newly applied Regulation C will inadvertently, but severely, damage an increasingly important portion of the market: the so-called "subprime" sector.

Our fundamental concern with the reporting regime outlined in the proposal is that it does not permit a meaningful inquiry into whether an institution's mortgage lending pricing policies and practices are rationally correlated to the risk factors of the mortgage loans being made—the data will not include the controlling factors that make up the cost equation.[1] We believe that this shortfall will permit industry detractors to draw erroneous conclusions concerning risk-based pricing of mortgage loans. HMDA does not permit the examination of whether price is correlated to the actual risk of the loan. This gap will leave the industry open forever to claims that its prices are excessive and not related to risk—this is simply not true.

The distorted conclusions undoubtedly will serve to unfairly damage some lenders' reputations. In this highly competitive market, the potential damage done to a lender's reputation by mischaracterizing the correlation between the risk taken by the lender and the ultimate price of the loan will cause many legitimate lenders to exit the subprime market, and actually reduce the competitiveness of this market. Indeed, AFSA believes that this is the goal of many industry detractors.

The risks associated with HMDA reporting, particularly by subprime lenders, are great. The misuse of the data is likely to lead to a complete distortion of risk-based pricing and lead some to assert that certain companies make race-based decisions. Such a conclusion could create the erroneous judgment that lenders use a system that correlates race to cost.

This potential misperception should not be permitted to destroy the subprime mortgage lending market, and we believe that it is incumbent upon the Board to do everything it possibly can to discourage the misuse of the data, and thwart those who will undoubtedly attempt to characterize the data in a manner which furthers an ideological agenda to damage, or even destroy, the subprime mortgage lending market.

Misinterpretation of the newly-reported data is not a small matter. Looking at race and price without additional context may lead to a wide-based perception that race correlates to cost. It does not.

We are hopeful that the Board will do everything in its power to prevent the misuse of the data, up to and including public denunciations of subprime industry detractors who attempt to equate risk-based pricing with race discrimination. Additionally, we respectfully request that the Federal Reserve strongly recommend a statement to accompany any use of the data. This disclosure should read:

> "This information was gathered from a database that does not include several factors that are integral in determining the price of a loan."

The potential ramifications of the misuse of these data are great. We sincerely hope that the Federal Reserve Board will help blunt misunderstanding of what the data represents, by strongly recommending the above disclaimer be associated with use of the data, and by publicly denouncing misuse of the data.

We appreciate the opportunity to comment on the Proposed Amendments.

Sincerely,

H. R. Lively, Jr.
President and CEO
American Financial Services Association

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[1] HMDA data will not include FICO scores, APR, income stability, property value stability, interest rate, points and fees, loan-to-value ratio, or performance data. Indeed, it would be inappropriate for HMDA data to include all of the data on factors that go into the cost of a loan, because proprietary company risk-modeling could then be reverse-engineered.